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APR 30 2014

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ORIGINAL

IN THE MATTER OF THE APPLICATION OF THE
ARIZONA ELECTRIC POWER COOPERATIVE,
INC. FOR A HEARING TO DETERMINE THE
FAIR VALUE OF ITS PROPERTY FOR
RATEMAKING PURPOSES, TO FIX A JUST AND
REASONABLE RETURN THEREON AND TO
APPROVE RATES DESIGNED TO DEVELOP
SUCH RETURN

Docket No. E-01773A-12-0305

**AEPCO'S APPLICATION FOR
APPROVAL OF THE ECAR
PLAN OF ADMINISTRATION
AND TARIFF**

Pursuant to the Fourth Full Ordering Paragraph at page 21 of Decision No. 74173 (the "Rate Decision"), the Arizona Electric Power Cooperative, Inc. ("AEPCO" or the "Cooperative") files its Environmental Compliance Adjustment Rider ("ECAR") Tariff and Plan of Administration. AEPCO requests the Commission approve the ECAR mechanism.

As brief background, the Rate Decision approved AEPCO's request for a revenue decrease of \$4.3 million – resulting in a roughly 3% drop in total revenue requirement compared to the 2011 test year and a rate decrease for four of AEPCO's five Arizona member distribution cooperatives. Notably, AEPCO and its members supported that rate decrease in conjunction with the Commission's approval of AEPCO's ECAR proposal.

The ECAR surcharge mechanism is intended to "provide recovery of potential costs associated with future environmental compliance obligations..."¹ Most immediate among those obligations is AEPCO's ability to fund both capital and operating expenses necessary to meet the EPA's Regional Haze requirements at Apache Station. In doing so, AEPCO will maintain the

¹ Rate Decision, Finding 77.

1 viability of Units 2 and 3 and their power, as well as rate benefits to its member distribution
2 cooperatives and their retail members.

3 AEPCO has worked with Utilities Division Staff to address the issues set forth in Finding
4 of Fact No. 78 of the Rate Decision. We have reached agreement on all aspects of the ECAR
5 mechanism, save one exception – that being use of the ECAR to recover chemical expenses
6 incurred solely due to environmental regulation(s). AEPCO requests the Commission approve
7 chemical expense recovery through the clause for several reasons.

8 First, the ECAR is an appropriate mechanism for recovery of this narrowly defined
9 category of operating expenses because (1) it will be incurred solely as a result of environmental
10 regulation(s) over which the Cooperative has no control, (2) the expense is considerable and
11 ongoing and (3) the price of these chemicals purchased from others is variable and volatile.
12 Current estimates for the chemicals required to comply with the Regional Haze requirements
13 range from \$4 to \$6 million annually.

14 To place that amount in context, an annual chemicals cost of \$4 to \$6 million is two to
15 three times AEPCO's Commission-approved total annual operating margin of just under
16 \$2 million. Obviously, if these chemical costs are not approved for ECAR recovery, many of the
17 mechanism's benefits – including rate gradualism, regulatory efficiency and the timely recovery
18 of costs which are beyond the Cooperative's control – will be significantly impaired.

19 Finally, these chemicals are used in many industries, as well as power plants, worldwide.
20 Given this heavy demand, experts predict substantial price volatility for these chemicals –
21 another reason which justifies cost treatment through the ECAR surcharge mechanism.
22 Accordingly, AEPCO maintains that authorization to recover these specific expenses is in the
23
24

1 best interest of the Cooperative and its members and is also consistent with the rationale
2 supporting adjustor mechanisms approved by the Commission for other utilities.

3 For the foregoing reasons, AEPCO requests the Commission enter its Order approving
4 the ECAR Tariff and Plan of Administration, which are attached as Exhibits A and B,
5 respectively.

6 RESPECTFULLY SUBMITTED this 30th day of April, 2014.

7 GALLAGHER & KENNEDY, P.A.

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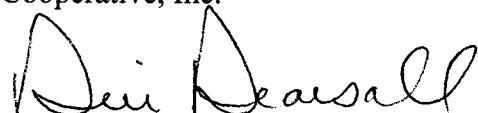
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10421-67/4178707

EXHIBIT A

ARIZONA ELECTRIC POWER COOPERATIVE, INC.

ENVIRONMENTAL COMPLIANCE ADJUSTMENT RIDER (ECAR)

TARIFF

Effective Date: May XX, 2014

PURPOSE

The purpose of the Environmental Compliance Adjustment Rider ("ECAR") is to provide a revenue recovery mechanism that will create a fund to be used for the purpose of meeting environmental compliance obligations mandated by federal, state, or local laws or regulations. The ECAR is the tariff collection mechanism for the overall Environmental Compliance Strategy ("ECS") developed by Arizona Electric Power Cooperative, Inc. ("AEPCO" or "Company") and its Members.

APPLICABILITY

Applicable to all Class A Member Distribution Cooperatives of AEPCO.

TERMS AND CONDITIONS

1. The initial rate of the tariff shall be set at zero. AEPCO will calculate the monthly dollar amount to be collected from each Class A Member Distribution Cooperative through the ECAR. AEPCO will allocate a portion of these costs to each Class A Member Distribution Cooperative based on the Allocated Capacity Percentage ("ACP") of each Member. The monthly dollar amount to be collected from each individual Collective All-Requirements Member ("CARM") will be based upon each CARM's monthly Demand Ratio Share. The Demand Ratio Share is calculated each month as the percentage of each CARMs' 12-month rolling average demand to the total of the CARMs' 12-month rolling average demand. AEPCO will also determine the term of collection for the costs. Once the monthly dollar amount for the fund and the term of collection have been established, AEPCO will file the ECS plan and a revised tariff with the Arizona Corporation Commission ("ACC" or "Commission"), for Commission approval.* Once the revised tariff is effective, each Member will be assessed a monthly charge on its bill in addition to other rates and charges approved by the Commission. Exhibit A sets forth the monthly Member charges and anticipated term of collection.
2. The level of funding and ECAR rates may be adjusted (up or down) depending on the actual environmental compliance funding needs of the Company as outlined in the ECS plan. Any changes to the ECS and ECAR tariff after the initial ECS plan is approved will be subject to a sixty (60) day ACC Staff review period.* The revised tariff shall become

effective at the end of the sixty (60) day period unless the Commission elects to suspend the revised tariff, in which case it shall become effective upon Commission approval.

Details of the operation of the ECAR and ACC compliance requirements are as set forth in the Company's Plan of Administration.

*In order for the ECAR to be revised, AEPCO must obtain Board approval and the unanimous consent of its Class A Member Distribution Cooperatives, prior to being submitted to the Commission.

EXHIBIT A

The Monthly Charge shall be as follows for each of the Company's Class A Member Distribution Cooperatives:

May XX, 2014*

Collective All-Requirements Members:

| | |
|--|------------|
| Anza Electric Cooperative, Inc. | \$0.00/mo. |
| Duncan Valley Electric Cooperative, Inc. | \$0.00/mo. |
| Graham County Electric Cooperative, Inc. | \$0.00/mo. |

Partial Requirements Members:

| | |
|--|------------|
| Mohave Electric Cooperative, Inc. | \$0.00/mo. |
| Sulphur Springs Valley Electric Cooperative, Inc. | \$0.00/mo. |
| Trico Electric Cooperative, Inc. | \$0.00/mo. |

*The stated Monthly Rate applies to service provided on and after this date.

EXHIBIT B

Arizona Electric Power Cooperative, Inc.

Environmental Compliance Adjustment Rider

Plan of Administration

ECAR – Plan of Administration

General Description:

The purpose of the Environmental Compliance Adjustment Rider (“ECAR”) Surcharge is to establish a fund to be used for the purpose of meeting, in whole or in part, the cost of environmental compliance obligations imposed on or applicable to the Arizona Electric Power Cooperative, Inc. (“AEPCO”) that are mandated by federal, state or local laws or regulations or judicial or regulatory agency interpretations of such laws or regulations (“Environmental Regulations”). The ECAR provides for the recovery of capital addition costs and any other costs specified in the Environmental Compliance Strategy, as approved by the Commission. The ECAR is not intended to recover any costs already recovered in base rates approved in Decision No. 74173 or any subsequent rate case decision or recovered through any other Commission-approved adjustor mechanism.

Key Definitions:

1. ECAR Surcharge – A rate rider approved by the Arizona Corporation Commission (“ACC” or “Commission”) in Decision No. XXXXX which authorizes AEPCO to: recover or mitigate Environmental Regulations operations’ costs; or fund, in whole or in part, capital additions required by Environmental Regulations.
2. Environmental Compliance Strategy (“ECS”) – A formal plan developed by AEPCO to meet Environmental Regulations. The ECS shall include, at a minimum, a scope of work, anticipated timelines and cost estimates.
3. Qualified Environmental Compliance Projects – Projects, as specified in the ECS plan, implemented in order to comply with standards mandated by Environmental Regulations. These standards include, but are not limited to, restrictions of carbon dioxide (CO₂), nitrogen oxide (NO_x), sulfur oxide (SO_x), ozone, particulate matter (PM), volatile organic compounds (VOC), mercury (Hg), and other toxins, coal ash and other requirements.
4. Qualified ECS Costs – The costs associated with Qualified Environmental Compliance Projects as identified in the ECS plan and approved by the Commission as appropriate for recovery through the ECAR Surcharge pursuant to ACC review of the ECS plan. The Qualified ECS Costs must be classified in one or more of the Rural Utilities Service (“RUS”) accounts, or any other successor RUS account, listed below under Qualified RUS Accounts. Any costs already recovered in base rates approved in Decision No. 74173 or any subsequent rate case decision or recovered through any other Commission-approved adjustor mechanism are not Qualified ECS Costs

1 and are not recoverable through the ECAR. Environmental fines or penalties
2 do not qualify for cost recovery through the ECAR Surcharge nor do costs
3 that have been included as part of AEPCO's authorized cost of service for
4 recovery through established rate tariffs.

5 **Calculation of ECAR:**

6 Based on costs detailed in the ECS, AEPCO will calculate the monthly dollar amount to
7 be collected from each Class A Member Distribution Cooperative through the ECAR.
8 AEPCO will allocate a portion of these costs to each Class A Member Distribution
9 Cooperative based on the Allocated Capacity Percentage ("ACP") of each Member. The
10 monthly dollar amount to be collected from each individual Collective All-Requirements
11 Member ("CARM") will be based upon each CARM's monthly Demand Ratio Share.
12 The Demand Ratio Share is calculated each month as the percentage of each CARMs'
13 12-month rolling average demand to the total of the CARMs' 12-month rolling average
14 demand. AEPCO will also determine the term of collection for the costs.

15 **Qualified RUS Accounts:**

16 The costs classified in the following RUS accounts are eligible to be recovered through
17 the ECAR. This list may be expanded to include other accounts approved by the
18 Commission in the future.

19 ***Steam Production Plant***

- 20 • 310 Land and Land Rights
- 21 • 311 Structures and Improvements
- 22 • 312 Boiler Plant Equipment
- 23 • 313 Engines and Engine Driven Generators
- 24 • 314 Turbogenerator Units
- 25 • 315 Accessory Electric Equipment
- 26 • 316 Miscellaneous Power Plant Equipment

27 ***Other Production Plant***

- 28 • 340 Land and Land Rights
- 29 • 341 Structures and Improvements
- 30 • 342 Fuel Holders, Producers, and Accessories
- 31 • 343 Prime Movers
- 32 • 344 Generators
- 33 • 345 Accessory Electric Equipment
- 34 • 346 Miscellaneous Power Plant Equipment

1 ***Steam Power Generation Operations***

- 2 • 502 Steam Expenses (limited to chemical expenses incurred solely due to
3 Environmental Regulation(s) but not including any indirect expenses such as
4 overhead)

5
6 **Accounting:**

7 Funds collected from the ECAR Surcharge will be separately identified by AEPCO and
8 recorded as a regulatory liability. Accounting for these funds shall be done on a
9 contributing Member Distribution Cooperative basis. Use of these funds to meet
10 Qualified ECS Costs will reduce that regulatory liability on a dollar-for-dollar basis.
11 Funds used for qualified environmental capital additions will be recorded as contributions
12 in aid of construction.

13 **Investment Administration:**

14 AEPCO will deposit all funds collected through the ECAR Surcharge in a separate
15 interest bearing investment account ("ECAR Surcharge Account") and may only draw
16 monies from the account to fund Qualified ECS Costs. Interest earned on the investment
17 of these funds shall be retained in the account. Upon completion or termination of the
18 ECS plan, all remaining funds in the ECAR Surcharge Account, including interest
19 earned, will be refunded to Members within ninety (90) days, returning the rates to zero,
20 using the same method established for the collection of the ECAR (see Calculation of
21 ECAR above).

22 **Compliance Reports:**

23 On September 1 for the previous January through June period and March 1 for the prior
24 year July to December period of each year, AEPCO will file semi-annual reports
25 concerning the ECAR Surcharge with the Commission, with a copy to its Members,
26 containing the following information for the reporting period:

- 27 1. The beginning balance of the ECAR Surcharge Account.
28 2. The amount collected from each Class A Member through the ECAR Surcharge,
29 including the total amount collected.
30 3. The total amount of interest earned by the ECAR Surcharge Account.
31 4. The total withdrawals for Qualified ECS Costs.
32 5. The ending balance of the ECAR Surcharge Account.

33 AEPCO will also file the following supporting information with the semi-annual report:

- 34 1. A listing of the dates and amounts of withdrawals.

1 2. A description of each Qualified ECS Cost paid during the period and the
2 accounting for each cost.

3 Each report will be certified by AEPCO's Chief Executive Officer or Chief Financial
4 Officer that all information provided in the filing is true and accurate to the best of his or
5 her information and belief. No compliance reports shall be required until after an ECS
6 plan is approved by the Commission. Once an ECS plan is completed or terminated and
7 any remaining funds have been refunded to Members and ECAR rates have been returned
8 to zero, AEPCO shall not be required to file compliance reports until the next ECS plan is
9 approved by the Commission.

10 **ECS and ECAR Surcharge Modifications:**

11 Pursuant to Decision No. XXXXX, the initial ECAR rate shall be set at \$0.00.
12 Thereafter, in response to an Environmental Regulation, AEPCO shall file its initial ECS
13 plan and a revised ECAR tariff with Docket Control for Commission approval.

14 The level of funding and ECAR rates may be adjusted (up or down) depending on the
15 actual environmental compliance funding needs of the Company as outlined in the ECS
16 plan. Any changes to the ECS and ECAR tariff after the initial ECS plan is approved will
17 be subject to a sixty (60) day ACC Staff review period. The revised tariff shall become
18 effective at the end of the sixty (60) day period unless the Commission elects to suspend
19 the revised tariff, in which case it shall become effective upon Commission approval.

20 Upon completion or termination of the ECS plan, all remaining funds in the ECAR
21 Surcharge Account not needed to meet the Company's objective(s) for the ECS plan,
22 including interest earned, will be refunded to Members within ninety (90) days, returning
23 the rates to zero, using the same method established for the collection of the ECAR.
24 AEPCO will file a revised tariff returning the rates to zero. The rates shall remain at zero
25 until AEPCO deems it necessary to utilize the ECAR tariff again in response to an
26 Environmental Regulation, in which case it will prepare and file an initial ECS plan and
27 initial revised tariff for Commission approval.

28 **AEPCO Board Approval and Member Consent:**

29 Prior to filing an initial ECS plan and revised ECAR tariff or seeking a subsequent
30 modification to either the ECS or ECAR, AEPCO will obtain authorization from its
31 Board. AEPCO shall also notify its Member Distribution Cooperatives sixty (60) days
32 in advance of a proposed filing with the Commission in order to confirm the unanimous
33 consent of its Members. Absent receipt of timely written objections, Member consent
34 shall be deemed obtained and AEPCO may proceed with the filing.